LOS ANGELES BAR BULLETIN

JR. BARRISTER'S ISSUE

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In This Issue

A Word from the Chairman of the Jr. Barristers . . . . *Robert M. Barton* 1

A Word from the President . . . *Clarence B. Runkle* 2

Payments to Deceased Partner's Estates—a Warning to Law Partners . . . . . . *Harold S. Voegelin* 3
(Prize Winning Article)

Work of 1949 Legislature—Editorial Board 5

Indemnification of Corporate Officers and Directors—Sec. 830, Corp. Code . . . . . . *Robert J. Cahall* 7

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VOL. 25 SEPTEMBER, 1949 No. 1

A WORD FROM THE CHAIRMAN OF THE JUNIOR BARRISTERS

Robert M. Barton

IT'S horn tooting time for the younger fellows. This issue is our bugle. We hope you will find the notes clear and the message informative. Perhaps you will even conclude that the wind used has been successfully converted to a kind of erudition.

The Junior Barristers Committee is enjoying a record rate of growth. Its activities are expanding correspondingly. So is its stature. For example, the number of articles submitted for this issue has far exceeded space allotment and previous experience. Some will probably appear in subsequent issues of the BULLETIN. The huge response is partially attributable to a contest held to determine the best article entered. Our judges have named Harold S. Voegelin the trophy winner. His work, appearing *infra* and entitled, "Payments to Deceased Partner's Estates — A Warning to Law Partners," merits your particular attention.

A good share of credit for the character of the material herein goes to special Junior Barrister Editor Chet Lappen and his board of associate editors. They put this number together and polished it. See their names on page 15. You will be hearing more of them.

Our post war progress as an organization is in large measure directly due to the efforts and abilities of Dolph Roome, Cam Cecil and Ed Jones, all former chairmen of the Junior Barristers, to the inspiration and attention of recent officers of the association, of men like Paul Fussell, Walter Nossaman, "Pat" Millikan and Clarence Runkle, to the generosity of the able lawyers who have

spoken at our luncheon meetings and to the encouragement of countless other members of the Bar.

The Junior Barristers Committee enthusiastically strives to be dynamic, responsible and constructive. We want to serve and be useful. Thank you for the opportunity.

ROBERT M. BARTON.

A WORD FROM THE PRESIDENT

We congratulate the Junior Bar on this fine issue of the BULLETIN which they have written and edited in its entirety, except, of course, these remarks.

The Association will hold a special luncheon meeting at the Biltmore Hotel on September 28th in honor of the Appellate Department of the Superior Court of Los Angeles County, presently composed of Judge Hartley Shaw, Judge Edward T. Bishop and Judge Jess E. Stephens.

The Court was established in September, 1929, and Judge Shaw and Judge Bishop have been on the Court continuously since that time. It would be difficult to find a Court in all the land that has earned and enjoyed higher respect and esteem of laymen and lawyers alike.

The program is being prepared by our hard working and very effective program committee under the able chairmanship of Grant Cooper.

Because of its civic nature, the meeting will be open to all the lawyers of the County. It will be held in the Renaissance Room, the larger rooms being unavailable on this date. I suggest that our members make their reservations promptly upon receipt of application forms, to insure getting tickets.

This significant celebration deserves a large attendance.

CLARENCE B. RUNKLE.

PAYMENTS TO DECEASED PARTNER'S ESTATES—A WARNING TO LAW PARTNERS*

Harold S. Voegelin**

Harold S. Voegelin

LAWYERS, in their pre-occupation with their clients' affairs, frequently are known to allow their own affairs to exist in a manner that is not the most desirable, or is not in their best interest. One example of this is partnership agreements between lawyers. While partners are generally forward-looking enough upon entering into such agreements to provide for the contingency of death of one of the partners, with provisions made for payments by the surviving partners to the deceased partner's widow or estate, they may not have considered the possible income-tax results of such an agreement.

Since the nature of a law practice necessitates the expenditure of a large amount of time and effort toward building of the firm's practice and the existence of work done on pending cases for which fees may not be received for some time, there may be at the time of a partner's death substantial amounts to which he is entitled but has not yet received, or to which he would eventually have become entitled. In order to avoid serious drain on the firm's finances in paying a deceased partner's interests in such items immediately upon his death, and in order to avoid complicated accounting problems, the partnership agreement usually provides for payments to be made over a period of time after the partner's death to his surviving widow or to his estate. The item that is likely to be overlooked is the necessity of drafting this agreement so that the portion of partnership income that is paid over to the deceased partner's widow is not required by the taxing authorities to be included in the taxable income of the surviving partner.

Unless this is done, the surviving partner may discover he is

*This article by Mr. Voegelin was selected as the best article on a current legal problem submitted in the recent Junior Barristers' contest.

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working for far less than he anticipated, after paying the deceased partner's share to the widow, and then paying income tax on the entire amount. A simple example illustrates the situation that can result.

Assume a two-man partnership netting the partners $50,000 per year, $25,000 each. Assuming both are married, their annual income tax will approximate $6,000, leaving each partner with $19,000 income after taxes. The partnership agreement provides that upon the death of one partner, the surviving partner will pay one-half the firm profits for the following two years to the decedent's widow. If such payments are taxed to the widow, the surviving partner still has his $19,000 income after paying the $6,000 tax on his $25,000 of firm income. The widow, assuming she doesn't remarry at once, pays $7,500 tax on the $25,000 paid to her. But if the entire firm income of $50,000 is taxed to the surviving partner, with no exclusion or deduction allowed for the $25,000 paid to the former partner's widow, the survivor will find himself paying income tax of $17,500 which, after paying one-half the firm income to the widow in compliance with the partnership agreement, will leave the surviving partner with a net income, after taxes, of $7,500.

Change this to a $100,000 partnership, with each partner netting $50,000 and the results can be even more disastrous. If the portion of income paid to the widow here is included in the survivor's income, the survivor may find his net income after taxes falling as low as $3,000. One can be assured in such a case that the surviving partner will be quite aggrieved indeed over the loss of the recently departed partner.

I.

The case of *Bull v. United States*[1] is generally regarded as the leading case in determining what should be done to avoid such a result. The case involved a ship brokerage firm which made payments to the estate of a deceased partner, as stipulated in the partnership agreement, and did not include such amounts in the taxable income of the surviving partners. In upholding the surviving partner's position, and finding the payments taxable to the deceased partner's estate, the Supreme Court pointed out the distinction between the surviving partners buying the deceased partner's interest, and the deceased partner's estate becoming in essence

[1]295 U. S. 247 (1935).

(Continued on page 9)

WORK OF 1949 LEGISLATURE

THE recently adjourned session of the California Legislature passed and sent to the governor a record number of 1713 bills. The governor signed 1603 of these and vetoed 30.

The editorial board[1] for the Junior Barristers' issue of the BAR BULLETIN has selected for brief comment what appear to be the more important changes of general interest contained in the 878 measures signed by the governor as of July 13, 1949. The greater part of these (pertaining to the Civil Code, Code of Civil Procedure, Probate Code, Corporations Code, Insurance Code, Labor Code (Workmen's Compensation), Banking Code, Health and Safety Code, and State Aeronautics Commission Act) appear throughout this issue of the BULLETIN; in each instance, unless otherwise noted, the changes are to be effective ninety days after the adjournment of the legislature—October 1, 1949.

The remaining comments (pertaining to the Revenue and Taxation Code, Business and Professions Code, Labor Code (General) and Welfare and Institutions Code), together with notation of measures signed by the governor subsequent to July 13, 1949, will be presented in a subsequent issue of the BAR BULLETIN.

AMENDMENTS TO CODE OF CIVIL PROCEDURE

C. C. P. Sec. 259(a) was amended by Chapter 469 to provide that court commissioner's findings in contested matters shall be signed immediately by the court, but that exceptions to commissioner's findings and to the court order thereon may be made within five days after written notice of the court's action. This bill became effective immediately.

C. C. P. Sec. 340 was amended by Chapter 863 by the addition of a new subsection (6), making the limitation period of one year applicable in an action against an officer to recover damages for the seizure of, detention of, or injury to the property seized for a statutory forfeiture to the State or for damages done to any person in making any such seizure.

C. C. P. Secs. 413, 1011, and 1012, and Probate Code Sec. 328 relating to service by mail were amended by Chapter 456 to broaden the definition of "post office" to include "mailbox, sub-post office, substation and mail shoot, or any other like facility

[1]The board wishes to acknowledge the assistance of Ernest Clark, James E. Dunlap, Franklin T. Hamilton, Ira Price, William Robertson, and James White in the preparation of this feature of the Junior Barristers' issue.

regularly maintained by the Government of the United States."

C. C. P. Sec. 542(5) was amended by Chapter 370 to provide that there shall be no liability upon the part of an attaching officer either to the plaintiff or the defendant for loss of any kind to personal property capable of manual delivery while in the possession of the attaching officer, unless the attaching officer shall be negligent.

C. C. P. Sec. 581(a) was amended by Chapter 463 to except from compulsory dismissal for lack of prosecution actions in which the parties file a stipulation in writing that the time may be extended.

C. C. P. Sec. 631.3 was added by Chapter 444 to provide for the forfeiture of jury fees deposited in the event of a settlement or a continuance which the court finds has occurred within sufficient time to notify the jurors that the trial would not proceed.

C. C. P. Sec. 673 was amended by Chapter 371 to provide that the court may direct the clerk to redeliver a writ of execution to the levying officer where the sale under such writ has been postponed beyond or not held within the return date of the writ so that the levying officer can make an alias return of the proceedings of the sale, or levy thereon as in the case of an original return of execution.

C. C. P. Sec. 690.24 was amended by Chapter 628 by increasing the exemption from execution for a motor vehicle from a value not exceeding $100 to a value not exceeding $250; an additional exemption for one house trailer actually occupied by the debtor and his family and of a value not exceeding $500 was added.

C. C. P. Sec. 690.26 was amended by Chapter 369 to extend the time for making a motion for a hearing on a claim of exemption for property under a writ of attachment or execution to five days after service on the defendant of a copy of the counter affidavit; it is further provided that property levied upon shall be released to the defendant if such a motion is not made within the time limited.

C. C. P. Sec. 1094.5 was amended by Chapter 358 to authorize a court reviewing an administrative order under writ of mandate to stay the operation of the administrative order until the expiration of time for filing notice of appeal, instead of merely until the court's judgment. If such a stay is in effect when a notice of

(Continued on page 27)

INDEMNIFICATION OF CORPORATE OFFICERS AND DIRECTORS—SCOPE OF SECTION 830 OF CORPORATION CODE*

By Robert J. Cahall**

THE story of the internecine warfare between shareholders and corporate management, of the weapons and defenses developed for the purpose, has been told often and ably.[1] Briefly summarized, the shareholders' derivative action, developed in equity to fulfill the need for protective measures against marauders in managerial posts, was sometime abused as a blackmail device for private gain. Efforts to limit the personal cost of defending such actions by directors and officers took two courses: (a) Indemnity provisions for such expenses were, either with[2] or without express legislative blessing, incorporated into by-laws or articles of incorporation, or, in some cases, into simple agreements with the corporation, or (b) By legislative intervention, the duty to indemnify for such expenses was imposed directly upon the corporation.[3]

Some of these indemnity provisions went beyond the fair limits of obligation to the directors,[4] and rather than to leave the matter to be worked out in the courts, California draftsmen devised what is now Section 830 of the Corporations Code to counter abuses in such indemnity provisions.[5]

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*This article by Mr. Cahall was selected by the judges, in the recent Junior Barrister essay contest, as worthy of special note.

**Mr. Cahall was born in Mansfield, Ohio, in 1919, and received his A.B. from Swarthmore College, Swarthmore, Pa., in 1941, and his LL.B. from Harvard Law School in 1947—after having had his legal education interrupted from December, 1942, until March 1946, during which time he served in the Army of the United States. He is a member of the L. A. Bar Association and is associated with the firm of O'Melveny & Myers.

[1] Ballantine, *California's 1943 Statute as to Directors' Litigation Expenses: An Exclusive Remedy for Indemnification of Directors, Officers and Employees,* (1943) 31 CALIF. L. REV. 515; Comment, *Right to Attorney's Fees in Shareholders' Derivative Suits,* (1942) 30 CALIF. L. REV. 667; Hornstein, *Directors' Expenses in Stockholders' Derivative Suits,* (1943) 43 COL. L. REV. 301; Hornstein, *New Aspects of Stockholders' Derivative Suits,* (1947) 47 COL. L. REV. 1, 8-11; Jervis, *Corporate Agreements to Pay Directors' Expenses in Stockholders' Suits,* (1940) 40 COL. L. REV. 1192; Washington, *Litigation Expenses of Corporate Directors in Stockholders' Suits,* (1940) 40 COL. L. REV. 431.

[2] CONNECTICUT (Gen. Stat. (1949), c. 249, Sec. 5129); DELAWARE (Rev. Code (1935), c. 65, Sec. 2034 (10)); MAINE (Rev. Stats. (1944), c. 49, Sec. 23); MICHIGAN (Gen. Corp. Act, Sec. 10, 1931 Stats. c. 327, Sec. 450.10); NEW JERSEY (L. 1942, c. 124); NEW YORK (Gen. Corp. Law, Sec. 63, 23 Consol. Laws, Sec. 63); WISCONSIN (Gen. Corp. Law, Sec. 182.01, Stats. (1933), c. 182, Sec. 182.01).

[3] KENTUCKY (Ky. Acts (1942), c. 40, Sec. 1, Gen. Corp. Law, (1946), Sec. 271.375); MONTANA (Civil Code, c. 15, Sec. 5942.2); NEW YORK (Gen. Corp. Law, Sec. 64, 23 Consol. Laws, Sec. 64); PENNSYLVANIA (12 Pa. Ann. Stat. (Purdon), Sec. 1323).

[4] See Note 16 *infra.* No case has been discovered passing on the validity of such by-laws as grant indemnity where a director or officer has been guilty of dereliction of duty but because of procedural defects in the complaint was not so adjudged.

[5] Adopted in 1943 as Section 375 of the CAL. CIVIL CODE.

STATUTORY INDEMNITY

Section 830 departs in many particulars from the statutory pattern of indemnity adopted in at least ten other states,[6] but, within the area of its operation, imposes liability directly upon the corporation for expenses incurred in such defense.[7]

It is proposed to outline the provisions and purposes of Section 830 and to designate some areas of conflict with pre-existing principles of law created by its language.[8]

A. *Outline of Statute*—Section 830 may be briefly summarized as follows:

(1) It applies to all actions, whether brought by the corporation, shareholder, governmental body or private person or corporation, in which a person is sued because of his present or past relationship as officer, director or employee of a corporation, domestic or foreign, in any proceeding arising out of his alleged official misfeasance or nonfeasance or out of any illegal wrongful act against or by the corporation.

(2) It confers upon such defendant a right of indemnity for the amount of such expenses incurred in his defense, including fees of attorneys and others, as the court hearing the matter may find to be reasonable.

(3) It provides for the enforcement of such right of indemnity against the corporation in the same or a separate proceeding only if (a) defendant is successful in whole or in part, or the action is settled with court approval, and (b) the court finds defendant's conduct fairly and equitably merits such indemnity.

(4) It authorizes the application for indemnity by defendant or persons supplying services, even though not parties to the action. (Notice of such application must be given to all parties to the litigations as well as to the

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[6]See Notes 2 and 3, *supra*.

[7]The full impact of this liability will probably be softened to a degree not yet determined by the new Section 834 of the Corporation Code (Statutes 1949, Ch. 499), which requires plaintiffs in derivative shareholders' actions, under certain conditions there specified, to furnish security for reasonable expenses, including attorney's fees and such other expenses as the corporation might be liable to pay under Section 830.

[8]Space will not permit development of what appear to be real problems of constitutional law and conflict of laws raised by this section. Because the section purports to apply to foreign corporations incorporated in states where such indemnity agreements may be expressly authorized (see Note 2, *supra*), the fact that foreign corporations may not transact business in California under more favorable conditions than domestic corporations does not satisfactorily dispose of the impairment of contracts argument as applied to presently existing agreements, by-laws or articles. Furthermore, there appears to be a real possibility of evading the limitations of Section 830 by separate actions brought outside of California to enforce indemnity agreements lawful where made or authorized by the state of incorporation.

(Continued on page 17)

PAYMENTS TO DECEASED PARTNER'S ESTATE

(Continued from page 3)

a member of the partnership for a period and as such sharing in the partnership income. Where it is found to be the former, the so-called "purchase" rule is applied, and the surviving partners are regarded merely as making a capital expenditure in making payments to the decedent's estate, and, accordingly, are taxed on the entire partnership income. Where the payments to the estate are determined to be income to the estate, the case is then under the so-called "income" rule, and the amount of the payments are excluded from the surviving partners' taxable income.

In determining that the partnership in *Bull v. U. S.* came within the "income" rule, the court placed emphasis on the fact that there was very little capital investment in the firm that the survivors could be purchasing from the decedent, a factor that law partnerships can generally comply with. In addition, the fact that payments were to be a continuation of the decedent's usual share of firm earnings after his death, rather than a stipulated set amount, or an amount based on a percentage of earnings for a set period prior to his death, was an added basis for applying the "income" rule.

Unfortunately, there has not been any particular consistency in the application of these two rules by the courts subsequent to *Bull v. U. S.* In 1937, the Board of Tax Appeals had before it the case of *W. Frank Carter v. Commissioner.*[2] This case involved a law partnership agreement providing for payments for a period of one year to the estate of a deceased partner. Despite the absence of any substantial capital investment in the firm in which the decedent could have had an interest, the "purchase" concept was applied to these payments and they were required to be included in the taxable income of the survivors. Such result can be attributed primarily to the fact that the payments were to total a sum equal to one-half the deceased partner's share in the partnership earnings for the two years preceding his death (in other words, a fixed sum as of the time of his death) and further, to the fact that the partnership agreement contained recitals that such payments were in discharge of the deceased partner's interests in the firm assets.

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[2]36 B. T. A. 60 (1937).

In more recent times, the year 1942 saw a case in which surviving law partners were held taxable on the amounts paid to a deceased partner's estate. This was the case of *Estate of George R. Nutter,*[3] in which a partner's regular percentage of firm profits was paid to his estate for an eighteen-month period following his death. The Court's basis for applying the "purchase" concept here is easily found inasmuch as the portion of the partnership agreement providing for these payments unfortunately specifically provided that they were in payment of the decedent's interest in "the capital, the assets, the receivables, the possibilities and the good will of the firm."

The most recent case in which the "purchase" concept was applied, to the dismay of the surviving partners, is *Raymond S. Wilkins v. Commissioner.*[4] The case is of importance because it appeared that the partnership articles providing for payments to the estate of a deceased partner were drafted with the specific thought of preventing just such a result. The agreement stipulated that in the event of the death of any partner, the partnership was not to be deemed dissolved, and it expressly stipulated that the partnership was not to be deemed to have any good will. However, in setting forth the amount to which the decedent's estate was to be entitled, the agreement, similar to the one in the *Carter* case,[5] provided for a sum equal to one-quarter the deceased partner's share of firm profits for the two-year period prior to his death to be paid to his estate within one year after his death. The court felt the presence of such a liquidated sum smacked too much of the idea of a purchase, and hence again included such sum in the taxable income of the survivors. The court did admit, however, that apparently all the survivors had purchased from the decedent was his interest in firm receivables accrued as of the time of his death, and that as these amounts were actually received, the survivors could exclude them from income until the amount of the payment to the decedent's estate had been recouped.

II.

As for cases applying the "income" concept to such payments, a series of three important cases in 1946 might be noted. The

[3]46 B. T. A. 35 (1942); affirmed, 131 Fed. (2d) 165 (C. A. 1st, 1942).
[4]7 T. C. 519 (1946); affirmed, 161 Fed. (2d) 830 (C. A. 1st, 1947).
[5]Note 2, *supra.*

first of these is *Estate of Frederic C. Bellinger,*[6] wherein the partnership agreement provided for the estate of a deceased partner to share in the profits of the firm for two years after his death to the same extent the partner would have shared, had he been living. The negativing of any "purchase" concept, and the application of the "income" concept, was made easy here inasmuch as the partnership agreement expressly provided that three named persons, none of them the decedent, were the owners of all the assets, receivables, and choses in action of the firm, and the decedent had agreed that he had no claim in regard to such items. On this basis, the court found the cases applying the "purchase" concept distinguishable.

Charles F. Coates v. Commissioner,[7] involving an accounting partnership, is a highly informative case applying the "income" concept. The partnership agreement here provided for payments of a stipulated percentage of partnership earnings for a period of five years to the estate of a deceased partner. The partnership agreement in question contained many provisions pointing toward the applicability of the "income" concept rather than the "purchase" concept, such as a provision that on the death of a partner the partnership should not be terminated thereby but was to continue with the decedent's estate as a partner for the five-year period, and a separate provision for payment to the decedent's estate for decedent's interest in accounts receivable and work in process at the time of his death. More important, the court recognized that the capital investment in a personal service partnership is small, as is also the good will factor.

The *Coates Case* was followed shortly by *John G. Madden v. Commissioner.*[8] The application of the "income" concept to the payments by the surviving partners to the deceased partner's widow in this case evidences a distinct trend of the Tax Court toward more liberality in applying the "income" concept. Here the payments to the widow were set at the fixed sum of $500 per month for a period of four years after decedent's death. Despite the presence of this liquidated sum, the court was of the opinion that the element of purchase and sale was not present, stating that, when the agreement was made, capital assets and good will were never considered, contemplated, or discussed and

[6] 5 T. C. M. 90 (1946).
[7] 7 T. C. 125 (1946).
[8] 5 T. C. M. 559 (1946).

were valueless for sale purposes. The *Wilkins* case was not mentioned.

The latest case in which the question has been litigated is *Sidney Hess v. Commissioner,*[9] decided May 13, 1949, involving a partnership of manufacturer's representatives. The partnership agreement contained certain somewhat confusing provisions as to whether the survivors were making a purchase of decedent's interest, or whether his estate was sharing in the income. The Commissioner attempted to include the payments in the income of the survivors under the "purchase" concept, resulting in the subsequent litigation. Among the questionable provisions were one providing that in no event was the estate of a deceased partner to be considered a partner, and another stating that the payments were being made for the use of the firm name. The Tax Court ultimately sustained the surviving partners' claim that the "income" concept should be applied, although three judges dissented. The majority judges decided from the testimony of the surviving partners that the recital that "payments were being made for use of the firm name" was set forth, not because the survivors considered they were buying any interest of decedent in such name, but because the partners had felt that such a recital was necessary in order to establish consideration for their agreement, and to bind the survivors to make the payments to the decedent's widow. This case also represents a definite advance of the income concept inasmuch as the payments to the decedent's widow were to continue for so long as she lived, if the survivor remained in the same type of business.[10]

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[9]12 T. C. No. 103 (1949).

[10]Other cases in which the question has been litigated since *Bull v. U. S.* are:
Applying the "purchase" concept: *Commissioner v. Smiley,* 86 Fed. (2d) 658 (C. A. 2d, 1936) (hotel business); *Estate of Bavier C. Miller,* 38 B. T. A. 487 (1938) (insurance); *Lyman M. Drake,* Para. 38,328 P-H Memo Dec. (1938) (insurance); *Edwards v. Commissioner,* 102 Fed. (2d) 757 (C. A. 10th, 1939) (tobacco brokers); *H. Lewis Brown,* 1 T. C. 760 (1943), *affd.* 141 Fed. (2d) 307 (C. A. 2d, 1944) (law firm); *Autenreith v. Commissioner,* 115 Fed. (2d) 856 (C. A. 3rd, 1940) (merchandising firm); *Lawrence W. Zonsius,* Para. 41,313 P-H Memo Dec. (1941) (insurance); *Estate of William T. Jones,* Para. 44,028 P-H Memo Dec. (1944) (law firm).

Applying the "income" concept: *Degener v. Anderson,* 77 Fed. (2d) 859 (C. A. 2d 1935) (business not stated); *Walter T. Gudeon,* 32 B. T. A. 100 (1935) (insurance); *Darcy v. U. S.,* 15 F. Supp. (Ct. Cl., 1936) (cotton brokers); *Helvering v. Smith,* 90 Fed. (2d) 590 (C. A. 2d, 1937) (law firm); *Richard P. Hallowell,* 39 B. T. A. 50 (1939) (merchandising firm); *Seavey & Flarsheim Brokerage Co.,* 41 B. T. A. 198 (1940) (food brokers); *Helvering v. Enright,* 312 U. S. 636 (1941) (law firm); *Herbert W. Kelley,* Para. 42,544 P-H Memo Dec. (1942) (manufacturing); *J. D. Trelfall,* Para. 44,157 P-H Memo Dec. (1944) (agency); *Frank R. Malloy,* 5 T. C. 1112 (1945) (undertaking firm); *Estate of Thomas F. Remington,* 9 T. C. 99 (1947) (insurance); *Boston Safe Deposit & Trust Co. v. U. S.,* 75 F. Supp. 884 (1948) (insurance); *Gussie K. Barth,* 35 B. T. A. 546 (1937) (law firm).

In addition to the above, there is the case of *G. Elliott Krusen,* Para. 44,287 P-H Memo Dec. (1944), affd. 148 Fed. (2d) 210 (C. A. 3rd, 1945), in which the

III.

With such an array of cases before him, the attorney who sets out to draft a partnership agreement that is to include provisions for payments to the estate of a deceased partner might well give consideration to the problem of avoiding the inclusion of such payments in the taxable income of the survivor. At the same time, the draftsman must keep in mind the interests of a deceased partner's widow and family, since they should be given some assurance that payments in the intended amount will actually be received.

Probably the best solution would be an amendment to the tax laws to provide definitely that the "income" concept be applied in all cases where payments are being made by a personal service partnership to the estate of a deceased partner. The Treasury has already made this specific recommendation to the Congress.[11] Section 109 of the Revenue Revision Bill of 1948 included such a provision in the proposed amendments to the Internal Revenue Code.

However, until final passage of such measures, the burden still falls on the draftsman of the partnership agreement to accomplish the same result by careful draftsmanship. The discussion of the foregoing cases suggests the following ten points for consideration in attempting to insure that the Commissioner will have no basis for refusing to exclude payments to the decedent's estate from the taxable income of the survivor:

(1) Studiously avoid any language in the general provisions of the agreement that would indicate a purchase or sale. Use of such words as "purchase," "sale," "interest," or "asset" should be avoided, and use should rather be made of such words as "share of income," "profits," or "earnings."

(2) Recite the purposes of the agreement to be to provide compensation to the deceased partner's estate for services rendered by the decedent to the firm prior

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court waived aside both the "income" and the "purchase" concept, found that the income in question was due solely to the efforts of the survivor, that he had no legal obligation to make payments out of it to the deceased partner's widow, and hence the entire amount was taxable to such surviving partner.

For general discussion of the problem, see M. S. Schiller, *The Lawyer's Dilemma*, 24 TAXES (The Tax Magazine) 837 (Sept. 1946); A. R. Cutler, *Income Tax Consequences Following the Death or Withdrawal of a Partner*, 28 BOSTON U. L. REV. 7 (Jan. 1948); G. J. Laikin and L. R. Lichter, *Survivor-Purchase Agreements*, 26 TAXES (the Tax Magazine) 931 (Oct. 1948).

[11] Letter of the Under Secretary of the Treasury, A. L. M. Wiggins, to Harold Knutson, Chairman, Committee on Ways and Means, Proposal No. 10 (February 26, 1948).

to his death, and to assure his estate a share in the profits of the firm to which the decedent would have been entitled had he lived.

(3) Consideration for the agreement should be made the partner's mutual undertakings to make the payments to the other partner's estate, and not the relinquishment by a partner of any claim or interest.[12]

(4) If there actually are substantial capital assets in the partnership, this should be recognized and a separate specific provision made for payment for the deceased partner's interest in them.

(5) If there is any likelihood of the Commissioner being able to establish good will as an asset of the firm, separate provisions should be made for paying decedent's estate for its interest in such good will.

(6) Payments to the deceased partner's estate should be in the form of a percentage of firm profits during the period the payments are to be made rather than a fixed amount. However, here the interests of the decedent's estate are directly contrary, and there may be a strong desire on the part of the partners to provide for at least a minimum payment to their estates. Although the requirement that a fixed sum be paid to the estate has been the occasion in the past for applying the "purchase" concept,[13] the *Madden Case*[14] permitted the "income" concept even though the agreement provided for payments of a fixed amount per month for a period of four years. However, even in that case, the agreement provided that the payments were to be made only if the earnings of the firm permitted.

(7) If feasible, the estate should be made a partner in the firm. An express stipulation that the estate is to share in losses as well as in the profits of the firm would point strongly toward the application of the "income" concept.[15] Here again, the best interests of the estate may be against this, if there is any like-

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[12]Although the *Krusen Case*, Para. 44,287 P-H Memo (1944), did not appear to accord such mutual obligations any weight as valid consideration, it was probably because of the particular circumstances of that individual case. The *Coates Case*, 7 T. C. 125 (1946), does clearly recognize such mutual obligations, and in so doing, was quoted with approval in the recent *Sidney Hess Case*, 12 T. C. No. 103 (1949).

[13]*Carter v. Commissioner*, 36 B. T. A. 60 (1937); *Wilkins v. Commissioner*, 7 T. C. 519 (1946).

[14]5 T. C. M. 559 (1946).

[15]There seems to be little doubt as to the validity of such a provision as to partnerships in general. See 20 CAL. JUR. 794; 47 CORPUS JURIS 1069; 50 YALE L. J. 202; 46 MICH. L. REV. 970. In the case of law partnerships such a provision would have to be expressly for purposes of income division only.

lihood that there may actually be losses[16] (not likely, of course, in the case of law partnerships).

(8) Recite in the agreement an understanding by the partners that such payments will be taxable income to their estates and that their estates are accordingly to pay the applicable tax on them.

(9) Upon the death of a partner and the making of the payments, it should be seen to that the deceased partner's estate actually reports the receipt of such income.

(10) As a final safety precaution to the surviving partner, the execution of a separate indemnity agreement by each partner might be suggested. This would provide that if, after the payment by the estate of income tax on the partnership payments received by it, the taxing authorities should succeed in taxing such payments in the income of the survivor, the estate will then immediately institute proceedings for a refund of the tax paid by it on such payments. Upon receipt of such refund, it would then be paid over to the surviving partner.[17] Such an agreement would, of course, usually be only a partial indemnity, since the additional tax imposed on the survivor, who is in higher brackets, would exceed the amount of tax originally paid by the estate. However, it would serve to relieve somewhat the situation in which the survivor might otherwise find himself by having to pay a tax on all of the partnership income.

[16] The agreement in the *Coates Case, supra,* contained an express stipulation that the estate was not to share the losses, which apparently did no harm. The *Sidney Hess Case, supra,* indicates it is not necessary that the estate be given any voice in the management of the firm.

[17] Receipt of such funds by the surviving partner would have no income tax consequences to such survivor, inasmuch as it would merely be a return of funds which he had already been required to report as income.

INDEMNIFICATION OF OFFICERS AND DIRECTORS

(Continued from page 8)

corporation, and, at the discretion of the court, to the shareholders of the corporation.)

(5) The rights and remedy conferred by the section are exclusive and no litigation expenses are recoverable in any action, no matter how terminated, except pursuant to the above court order, nor shall such indemnity be in any way governed by articles, by-laws or indemnity agreements of the corporation, its directors or shareholders.

Eschewing the concept that defense of actions by corporate officers, directors and employees is of such benefit to the corporation that reimbursement for litigation expenses should be allowed,[9] the draftsmen based this statute upon the theory "of a duty of a principal to indemnify and reimburse his employee or agent for expenses springing from the proper performance of the duties of his employment."[10]

B. *Actions to Which Applicable*—As can readily be perceived, the section is made applicable to the widest conceivable area of litigation in which a relationship between an officer, director or employee and his corporation is involved. Questions running the gamut of legal complexity from participation in a conspiracy to restrain trade to the simple question of principal-agent relationships are included in its scope. It would appear to cover criminal as well as civil actions. It is not designed to permit indemnity for litigation expenses incurred in suits based upon the actions of defendant acting in the role of private individual.[11] However, in situations where defendant's liability depends upon the finding that he acted in his official capacity rather than as a private individual untrammeled by fiduciary duties, as in the "corporate opportunity" cases, it would appear that, although he successfully establishes the fact that in so acting he was *not* acting as a director, officer or

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[9]*Mann v. Hearst*, L. A. Super. Ct. No. 432, 229 (Sept. 1941); *Singh v. United States Malwa Sudharak Society*, 5 Cal. (2d) 405 (1936); *Wickersham v. Crittenden*, 106 Cal. 329 (1895); *Godley v. Crandall & Godley Co.*, 168 N. Y. S. 251 (App. Div. 1917); *Esposito v. Riverside Sand & Gravel Co.*, 191 N. E. 363 (Mass., 1934); *contra, Re Hutto Eng. Co.*, 246 N. W. 172 (Mich. 1933); *Solimine v. Hollander*, 19 A. (2d) 344 (N. J. Eq. 1941).

[10]BALLANTINE & STERLING, CALIFORNIA CORPORATION LAWS (1949 ed.), Sec. 95, p. 121.

[11]See WASHINGTON, CORPORATE EXECUTIVES' COMPENSATION (1942), pp. 420-421, for comments on similar language in what is now Section 63 of N. Y. Gen. Corp. Law, which confers the right of indemnity in "any action, suit or proceeding in which he [the director] is made a party by reason of his being or having been a director of the corporation."

employee, he was "sued . . . because he is or was a director . . . of a corporation" within the meaning of Section 830. Since no published reports have been found on this or any other facet of the section, the question of outer limits of applicability must be left to future determination by the courts.

The section extends rights of indemnity to employees upon the reasoning that "there seems to be no reason to withhold indemnity from employees other than officers, as the line between officers and such executive employees as managers may be difficult to draw."[12] The draftsmen apparently felt that the language of Section 2802 of the California Labor Code[13] was ineffective to accomplish the desired result. To some extent, however, there would appear to be some duplication in coverage, the consequence of which will be later examined.

C. *Limitations on Indemnity*—Notwithstanding the broad applicability of Section 830 to litigation of widely varying types, corporate officials have viewed with concern the restrictive provisions in the section which render such breadth of coverage a mixed blessing. In the first place, to be entitled to indemnity, the defendant must be "successful in whole or in part"[14] or he must have achieved a settlement approved by the court, and his conduct "fairly and equitably merit[s] such indemnity." In the second place, as specifically stated therein, "the rights and remedy provided . . . are exclusive." Further, contracts and agreements of indemnity, article and by-law provisions and resolutions upon which corporate officials have learned to rely in the past decade for protection from strike suits and from imposition of personal liability in other types of litigation are expressly superseded by the section.[15]

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[12] BALLANTINE & STERLING, *op. cit.*, pp. 121-122.

[13] "Sec. 2802. *Indemnification of employee for expenditures or losses in discharge of duties or obedience to directions.* An employer shall indemnify his employee for all that the employee necessarily expends or loses in direct consequence of the discharge of his duties, as such, or of his obedience to the directions of the employer, even though unlawful, unless the employee, at the time of obeying such directions, believed them to be unlawful." This section has not been applied in California to corporate executives or directors, although its principles appear to be applicable in certain instances. One basis for reconciling this section with Section 830, suggested by Ballantine & Sterling (see Note 12, *supra*) is to apply 830 only to executive employees, so as to leave undisturbed the law of master and servant.

[14] Section 830(a)(1). For interpretation of the meaning of this and similar language, see BALLANTINE & STERLING, *op. cit.*, p. 119; Hornstein, *Directors' Expenses in Stockholders' Suits*, (1943) 43 COL. L. REV. 301, 313.

[15] Section 830(e) reads as follows: "The rights and remedy provided by this section are exclusive. The awarding of indemnity for expenses, including attorneys' fees, to parties to such proceedings, whether terminated by trial on the merits or by settlement or dismissal, shall be made only upon order of court pursuant to this section, and shall not be governed by any provision in the articles or by-laws of the corporation or by resolution or agreement of the corporation, its directors, or its shareholders."

Professor Ballantine, one of the draftsmen of this legislation, states that the policy behind this last provision was to eliminate all such article and by-law indemnity provisions because there were some of these which went further than sound policy would permit.[16] Some of these provisions permit indemnity in all cases except where a director or officer is finally adjudged liable for wilful misconduct. In such cases, the right to indemnity would include amounts paid in settlements and expenses of procuring dismissals on procedural grounds alone, regardless of the culpability of the defendant. Although such provisions may well be held void, in whole or in part, as violative of public policy, limitations imposed upon indemnity agreements at common law, large sums may be disbursed prior to a final determination of their invalidity, and said sums may never be recovered by the corporation.

Professor Ballantine concludes that "[i]f a jurisdiction decides to continue to allow such by-law provisions at all, some regulation should be adopted to limit pernicious blanket provisions which are so extreme as to be of doubtful fairness or legality . . . There are some legal disorders which cannot be cured by the poultice treatment but require a radical surgical operation. This was the view of those who drafted the California Act."[17]

D. *Extent to Which Contractual Indemnity Superseded*—The wording of this exclusory subsection raises some serious problems of construction with consequences perhaps not contemplated by its draftsmen. The first question to be considered is whether this particular subsection was intended to exclude indemnification for judgments on settlements, as well as litigation expenses. Following logically from the foregoing reasoning, such "radical surgical operation" as this statute purported to be might have excised all portions of such "pernicious blanket provisions" so that no part thereof would have to be submitted to the test of litigation to establish its invalidity. Nevertheless, under the literal wording of the act, this "exclusive" remedy was made applicable only to indemnity for "expenses, including attorneys' fees, to parties to such proceedings." This conclusion finds support in the language of subsection (a), which reads in part: "The amount of such indemnity shall be so much of the expenses, including attorneys'

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[16]Ballantine, *California 1943 Statute as to Directors' Litigation Expense: An Exclusive Remedy for Indemnification of Directors, Officers and Employers,* (1943) 31 CAL. L. REV. 515, 522.

[17]*Id.* at pp. 525-526.

fees, incurred in the defense of the proceeding, as the court determines and finds to be reasonable." It is clear that the draftsmen intended such limitation,[18] and apparently were content to let the courts pass upon the validity of indemnity provisions which grant relief for amounts paid in settlement and satisfaction of judgments.

CONTRACTUAL INDEMNITY

A. *Corporate Power*—Because there is an area within which public policy does not nullify such indemnity provisions, an examination of California law on the point is required. Any approach to this point should commence with an examination of the power of the corporation to make such provision in its articles or by-laws. Although the legislatures of other jurisdictions have seen fit to include express authority for such indemnification in the powers conferred upon domestic corporations[19] or to authorize the adoption of amendments of articles or by-laws providing for indemnity,[20] it is probable that California corporations have the power to make provision in its by-laws for indemnity of its officers and directors under Section 501 of the Corporation Code which provides in part:

> "The by-laws of a corporation may make provisions not in conflict with law or its articles for:
>
> (d) The number, qualifications, duties, and compensation of directors . . .
>
> (f) The appointment, duties, compensation, and tenure of office of officers other than directors.
>
> (k) Any other proper and lawful regulations."

It appears elementary that an undertaking to assume the risks of litigation attendant upon the lawful exercise of the powers of officers and directors is compensatory in nature.

Authority to make such provision in its articles, a more cumbersome procedure, is probably conferred under Section 305(c) of the Corporation Code which provides in part as follows:

> "The articles may include any desired provisions:
>
> (c) Imposing any limitations and requirements authorized by this division, and otherwise regulating the business and affairs of the corporation and the powers of

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[18] *Id.* at p. 517; BALLANTINE & STERLING, *op. cit.*, p. 124.

[19] DELAWARE (Rev. Code (1935), c. 65, Sec. 2034 (10)); MICHIGAN (Gen. Corp. Act, Sec. 10, 1931 Stats. c. 327, Sec. 450.10); WISCONSIN (Gen. Corp. Law, Sec. 182.01, Stats. (1933), c. 182, Sec. 182.01).

[20] CONNECTICUT (Gen. Stat. (1949), c. 249, Sec. 5129); MAINE (Rev. Stats. (1944), c. 49, Sec. 23); NEW JERSEY (L. 1942, c. 124); NEW YORK (Gen. Corp. Law, Sec. 63, 23 Consol. Laws, Sec. 63).

the directors and shareholders in a manner not in conflict with law."

The same result may be reached by applying the general principle that a corporation has the power to enter into a contract of indemnity whenever the transaction can reasonably be said to be beneficial to the corporation as an incident of the conduct of the business authorized by its articles.[21]

An alternative available to a corporation desiring to obtain the services of high-calibre personnel is to pay them an annual compensation commensurate with the responsibility and exposure to litigious complainants, incidental to such positions. By means of indemnity provisions, the cost of compensation can be precisely equated to the risk assumed and should be properly treated as a cost of carrying on the business of the corporation.[22]

B. *Policy Limitations*—The outside limits imposed by public

[21]*Rabbitt v. Union Indemnity Co.*, 140 Cal. App. 575 (1934); *Simpson v. Bergmann*, 125 Cal. App. 1 (1932); *Woods Lumber Co. v. Moore*, 183 Cal. 497 (1920).

These cases do not apply to the indemnity of corporate officials but rather to agreements entered into on behalf of customers of the corporations; the benefit to the corporation in obtaining experienced and qualified personnel in policy-determining and managerial positions would make such principle applicable.

[22]See Jervis, *Corporate Agreements to Pay Directors Expenses in Stockholders' Suits*, (1940) 40 COL. L. REV. 1192.

policy upon such indemnity agreements, without reference to additional limitations resulting from the fiduciary duties owed to shareholders, are codified in Sections 2773-2778 of the Civil Code. Section 2773 voids agreements to indemnify for acts to be performed in the future if the indemnitee, at the time of performance, knows his act to be unlawful. Section 2774 upholds agreements to indemnify as applied to actions in the past, even though known to be wrongful, unless such act was a felony.[23]

The probable limit imposed by public policy upon such indemnity provisions is affected by the fiduciary duty imposed on corporate officials. No recovery can be had upon the indemnity contract by one who suffered loss by reason of his own wrongful act.[24] The defendant director and officer in a shareholders' derivative suit is resisting allegations that he has breached his duties to the corporation and to its shareholders. Where there is such antithesis of interest between indemnitor and indemnitee, a blanket indemnity provision against the expenses of defense and judgments obtained not only violates concepts of justice and equity but also might well be void as a species of maintenance.[25] As a consequence, no recovery should be permitted for expenses incurred in an unsuccessful defense against a shareholder's derivative suit, and, *a fortiori,* for judgments or settlements[26] obtained pursuant to such suit against a delinquent officer or director.

OTHER BASES FOR INDEMNITY

There is, however, a wide area of law not involving the breach of fiduciary duty of officers and directors to the corporation and its shareholders where indemnity provisions would be clearly upheld. Indeed, under well-established principles of agency law, there is a duty on the part of the principal to indemnify for losses actually suffered (1) as a direct and natural consequence of the execution of the agency, (2) wherein the agent was innocent of negligence or knowingly unlawful conduct, and (3) where the

[23]Section 2778, supplying rules of interpretation for such contracts, provides in part: "3. An indemnity against claims, or demands, or liability, expressly, or in other equivalent terms, embraces the costs of defense against such claims, demands, or liability incurred in good faith, and in the exercise of a reasonable discretion." It is apparent that a square conflict between the foregoing language and that of Section 830 of the Corporation Code must be resolved in the favor of the latter upon the familiar basis of statutory construction that the specific governs the general.

[24]*Byron Jackson Co. v. Woods,* 41 Cal. App. (2d) 777 (1940). An exception to the rule has been made where the indemnitee has no knowledge, actual or constructive, that such act is wrongful. See Note 13, *supra,* and Note 26, *infra.*

[25]*British Cash & Parcel Conveyors v. Lamson Store Service Co.* (1908), 1 K. B. (Eng.) 1006, 14 Ann. Cas. 554; Jervis, *op. cit.,* p. 1192; Hornstein, *Directors' Expenses in Stockholders' Suits* (1943), 43 COL. L. REV. 313, 314; 10 AM. JUR., *Champerty and Maintenance,* Sec. 15, p. 561; 27 AM. JUR., *Indemnity,* Sec. 10, p. 461.

[26]See Hornstein, *op. cit.,* 43 COL. L. REV. at 313.

agent was acting within the scope of his authority.[27] Similar duties are imposed upon beneficiaries in favor of the trustee.[28]

In two cases agency principles were applied to the question of reimbursement of officers or directors for expenses incurred in litigation although recovery was denied the official. In *Hoch v. Duluth Brewing Malting Co.*, 217 N. W. 503 (Minn. 1928), recovery was denied because the officer director had failed to allege that the wrongful act for which he had been sued had been directed by the corporation, and that he had in good faith complied. In *Du Puy v. Crucible Steel Co. of Am.*, 288 Fed. 583 (W. D. Pa. 1923), no recovery was permitted because the officer had not alleged that the corporate income tax return filed by him, upon which the government based its unsuccessful prosecution for conspiracy to defraud, was correctly made out or that its errors were the result of honest mistake. Both cases come within well established exceptions to the rule, and there is no reason to believe from the result of these cases that the general agency principle would be inapplicable.[29]

IMPACT OF STATUTE ON INDEMNITY LAW

Section 830 of the Corporations Code purports by its language to cover litigation involving legal relationships where indemnity articles, by-laws and agreements are not only enforceable but are implied from the relationship between the corporation and its officers, directors and employees. As a consequence of the exclusory language[30] of subsection (e), any rights which corporate directors, officers and employees may have to indemnity for litigation expenses are now limited to those cases in which their defense has been "successful in whole or in part."[31] The net result is somewhat incongruous—an agent who has suffered a judgment because of wrongful conduct carried out in good faith on behalf

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[27] RESTATEMENT OF AGENCY, Secs. 438-439; MECHEM, AGENCY (2d ed., 1914), Sec. 1602, p. 1201; 1 CAL. JUR., *Agency*, Sec. 97, p. 813. See also Note 13, *supra*.

Space does not permit any detail of the substantive aspects of agency or trust law, but it appears pertinent to point out that such principles have been applied in a plethora of cases to officers and directors of a corporation. *McEwen v. Kelly*, 79 S. E. 777, 779 (Ga., 1913); 3 FLETCHER, CYCLOPEDIA CORPORATIONS (Rev. ed., 1947) vol. 3, Secs. 846-847.

[28] *Solimine v. Hollander*, 19 A. (2d) 344 (N. J. Eq., 1941); Scott, Trusts (1939), Sec. 188.5; CAL. CIVIL CODE, Sec. 2273.

[29] For a collection of cases on the proposition that an agent may recover litigation expenses incurred in defending the property or rights of his principal, and even the amount of the judgment obtained against him, see *Schwarting v. Artel*, 40 Cal. App. (2d) 433 (1940); *Admiral Oriental Line v. United States*, 86 F. (2d) 201 (C. A. 2d, 1936).

[30] See Note 15, *supra*.

[31] Where an agent successfully resists suit by his principal, he formerly had no right to recover expenses so incurred from his principal. This is now changed under Section 830 so that such recovery is permissible where his conduct was fair and equitable.

of his principal can still recover the amount of the judgment so recovered against him,[32] but he is barred from recovery of his expenses to defend the suit.

CONCLUSION

In summary, the draftsmen of Section 830 have substituted for contractual indemnity provisions, whether by agreement, resolution, by-law, or articles, a statutory remedy which conditions the right of recovery upon successful defense, in whole or in part, and upon fair and equitable conduct. This remedy is applicable to litigation expenses, and, by the same token, it is a substitute only for contractual indemnity provisions relating to litigation expenses. The section does not appear to abrogate provisions indemnifying officers and directors for the amount of settlements or judgments against them, but leaves such provisions to be tested as to validity by principles of common law. Indemnity provisions of such scope have been upheld at common law where the indemnitor and indemnitee have a community of interest and recovery of similar scope is a well established right of agents and

[32] BALLANTINE & STERLING, *op. cit.*, p. 124; see Note 29, *supra.*

trustees. As a consequence, the draftsmen have created the anomalous result that judgments against, and settlements by, officers and directors may be recoverable by them from the corporation but the expenses of litigation may not.

Within the relatively narrow field of shareholders' derivative actions, Section 830, with its prerequisites of successful defense and fair and equitable conduct, is consistent with sound policy. But in broadening its scope of applicability, it would appear that its draftsmen ventured into areas of the law already well charted, where by its exclusory feature they have abrogated any other remedy for the recovery of litigation expenses by corporate officials and employees. A solution to the problem would seem to require one of two courses—the narrowing of the scope of Section 830 to those actions in which internal corporate relationships are litigated, *i.e.*, shareholders' derivative suits, or the contraction of the exclusory clause, so as to make it clear that in furthering the business relationships of the corporation with outsiders, corporate officers and agents may safely rely upon contractual indemnity and upon similar rights available under agency and trust law.

1949 LEGISLATION

(Continued from page 6)

appeal is filed, the stay is extended by operation of law for twenty days from the date such notice is filed.

C. C. P. Sec. 1187 dealing with mechanics' liens was amended by Chapter 632 by the addition of a definition of the word "owner." A new paragraph was also added to the section providing that no extension of a lien or giving of credit shall be effective against a *bona fide* purchaser whose rights are acquired subsequent to the 90 day period following the filing of a lien unless notice of such extension or credit is recorded prior to the acquisition of the purchaser's rights. It is further provided that no proceeding to enforce a lien shall be effective to establish priority unless a notice of *lis pendens* is filed as provided in C. C. P. Sec. 409.

C. C. P. Secs. 2051 and 2065 were amended by Chapter 333 to prevent the impeachment of witnesses on the grounds of a felony conviction where the witness has previously received a full and unconditional pardon based upon a certificate of rehabilitation.

AMENDMENTS TO THE PROBATE CODE

Prob. C. Sec. 645 was amended by Chapter 453 to provide specifically that estates not exceeding $2,500 in value, which may be set aside to the surviving spouse or children, shall be valued at the date of death rather than at the date of hearing.

Prob. C. Sec. 754 was amended by Chapter 390 by the addition of a provision, stated to be declaratory of the pre-existing law, that the personal representative in making a sale of decedent's property may sell the entire interest of the estate in the property or any lesser interest.

Prob. C. Sec. 754.6 was added by Chapter 478 to clarify the status of leasehold interests for purposes of sale by providing that leasehold interests: (a) In real property with an unexpired term of ten years or longer, (b) in real property with an option to purchase the leased premises or some part thereof, (c) in oil or gas, shall be sold as real property of the estate; all other leasehold interests shall be sold as personal property.

Prob. C. Sec. 801 was amended by Chapter 455 to reduce from an amount double the unpaid payments to an amount equal to the unpaid payments, the bond required of a purchaser from an estate of a contract for the purchase of land.

Prob. C. Sec. 1080 was amended by Chapter 454 by adding a new requirement that a petitioner for determination of heirship must mail notice to designated persons at least ten days prior to date of hearing.

AMENDMENTS TO THE CIVIL CODE

C. C. Secs. 226(a) and (b) were added by Chapter 522 to provide that the consent of natural parents to the adoption of their child cannot be withdrawn without court approval upon a hearing on petition to withdraw consent at which the State Department of Social Welfare represents the child; prior case law was to the effect that a parent had the right to withdraw consent at any time before the adoption decree (*Adoption of McDonnell*, 77 C. A. (2d) 805).

C. C. Sec. 1881.3 was amended by Chapter 295 to extend the application of the private bulk grain storage sections from Dec. 31, 1949, to Dec. 31, 1951.

C. C. Sec. 2952 was amended by Chapter 443 to dispense with the necessity of recording an entire instrument where a portion of the instrument includes a mortgage or a deed of trust; under specified conditions, only the mortgage or deed of trust portion need be recorded.

C. C. Sec. 3370 was added by Chapter 652 to define "unfair competition" as used in C. C. Sec. 3369 to include any act denounced by the "Unfair Practices Act" in the Bus. & Prof. Code; however, any district attorney may prosecute for the violation of said "Unfair Practices Act" only as is provided in Article 6 of said Act, not C. C. Sec. 3369(5).

NEW BANKING CODE ENACTED

By Chapter 755, the legislature established a new Banking Code which consolidates, overhauls and revises the laws relating to banks and banking, trust companies and trust business, foreign banking corporations, the sale, merger, reorganization and dissolution of banks and trust companies and related subjects; the "Bank Act" (Chap. 76 of the Stats. of 1909) was repealed.

AMENDMENT TO THE HEALTH AND SAFETY CODE

H. & S. C. Sec. 24400 was amended by Chapter 136 to expressly recognize abandoned wells, septic tanks and cesspools as dangerous excavations and to provide that any landowner or person in possession of land is guilty of a misdemeanor if he permits the existence of an abandoned excavation "dangerous to persons legally on the premises, or to minors under the age of 12," and fails to keep

it covered or securely fenced; the section formerly covered only abandoned excavations dangerous to passers-by or livestock.

AMENDMENT TO STATE AERONAUTICS COMMISSION ACT

By Chapter 653, the legislature added Section 15 to the State Aeronautics Commission Act to provide that the liability of an airman for personal injuries or death of non-paying guests shall be limited to cases where the proximate cause was the intoxication or wilful misconduct of the airman. Chapter 654 added a section to provide a lien in favor of persons performing work on or furnishing supplies and materials for the repair or safekeeping of an aircraft.

AMENDMENTS TO THE INSURANCE CODE

Ins. C. Secs. 1610-1620, to be cited as the Unauthorized Insurers Process Act, were added by Chapter 495 to provide that the issuance or delivery of policies to residents of this state, the solicitation of applications for insurance contracts, and the collection of premiums, when effected in this state by non-admitted insurers by mail or otherwise, shall be equivalent to an appointment of the Insurance Commissioner as an agent for the service of process.

Ins. C. Sec. 10115 was added by Chapter 409 to provide that the full amount of a life insurance policy is payable although the policy is not issued at the time of death if there has been (1) an application, (2) payment of the first premium, and (3) approval of application by insurer; the insurer may limit the effect of this section by appropriate provision in the application.

Ins. C. Secs. 10170 and 10375 were amended by Chapter 307 to give the right to change the beneficiary of life insurance policy without consent of the beneficiary unless the rights of the beneficiary have been expressly declared to be irrevocable.

AMENDMENTS TO THE CORPORATION CODE

Corporation Code, Sec. 834, relating to derivative actions by shareholders, is added by Chapter Law 499 to the Corporation Code. This new statute creates a number of pleading and procedural restrictions upon the institution of derivative suits. They are, in general, as follows:

1. An allegation by the plaintiff of registered ownership at the time of the acts complained of.

2. An allegation, pleaded with particularity, of the plaintiff's efforts to secure action from the board of directors; an allegation

that he has informed the corporation in writing of the ultimate facts of each cause of action; and an allegation setting forth the reasons for his failure to obtain action from the board or his excuse for not having made such an effort.

3. A provision that a plaintiff, upon motion by the corporation or any defendant, may be compelled to furnish security for costs in such amount as may be determined by the court, and the further provision that the prosecution of the action shall be stayed until ten days after such a motion has been disposed of.

Corporation Code Sec. 3301 as enacted by Chapter Law 746 imposes the new requirement that all domestic corporations must file with the Secretary of State a statement listing the names of certain named principal officers, together with a statement of the location and address of its principal office. It further requires that changes of address or location of domestic corporations be reported to the Secretary of State together with a list of its then officers, and makes it clear that the designation of an agent to receive service of process by a domestic corporation is merely optional.

Corporation Code Secs. 15001-15700, inclusive, as enacted by Chapter Law 383, adds Title 2, Partnerships, to the Corporation Code. With the exception of Penal Code Sec. 358 and Chapter 129 of the General Laws of 1869-1870, these sections are comprised entirely of former Civil Code sections, being the Uniform Partnership Act and the Uniform Limited Partnership Act.

Section 15006, which was formerly Section 2400 of the Civil Code, subjects limited partnerships to the provisions of the act whereas previously it applied only to special and mining partnerships.

Section 15009 proscribes the authority of a partner in his relationship to persons dealing with the partnership. The act provides that unless authorized by other partners, or unless they have abandoned the business, one or more but less than all the partners have no authority to do any other act which would make it impossible to carry on the ordinary business of "a" partnership, whereas previously this limitation was restricted to the doing of any other act which would make it impossible to carry on the ordinary business of "the" partnership.

Section 15010.5 incorporates the definition of "conveyance"

from Section 1215 of the Civil Code as well as the previous definitions which were found in Section 2404 of the Civil Code.

In Section 15044, which distinguishes general partnerships from other types of partnerships and which was formerly Section 2438 of the Civil Code, the new act adds limited partnerships to special and mining partnerships as those distinguished from a general partnership.

Corporation Code Secs. 25000-26104, as enacted in Chapter Laws 384, 389 and 388, place the Corporate Securities Act in the Corporation Code.

Corporation Code Sec. 25154 was amended by Chapter Law 387 by adding the following sentence: "However, this section does not prohibit the transaction of business or the performance of any act, other than the issue or sale of securities by a corporation before it has applied for and received a permit to issue or sell securities, and has received a permit to issue or sell securities, and has issued shares in conformity therewith." This sentence clarifies the extent of activity which might be carried on by a corporation prior to the issue of stock.

Corporation Code Secs. 27000-27203, as enacted by Chapter Law 385, place in the Corporation Code the Security Owners' Protection Law.

Corporation Code Secs. 28000-28501, as enacted by Chapter Law 462, place in the Corporation Code the Retirement System Act.

Corporation Code Secs. 29000-29201, as enacted by Chapter Law 462, place in the Corporation Code the Bucket Shop Law of 1927.

AMENDMENTS TO THE LABOR CODE (WORKMEN'S COMPENSATION)

Labor Code Sec. 3856 is amended by Chapter Law 120. Where an employee recovers damages against a third party, and the employer has paid compensation to the injured employee, the employer is entitled to reimbursement out of such recovery for the compensation he has paid; but an amendment to Labor Code Sec-3856 now permits the employee to deduct his reasonable attorney's fees (as fixed by the Court) in cases where the employer has not joined or been represented in the action brought by the employee against the third party.

Labor Code Sec. 3863 is added by Chapter Law 120. The new section expressly recognizes the right of an employee and his attorney to contract as between themselves for attorney's fees in any action or claim brought by the employee against a person other than his employer.

Labor Code Sec. 5801 is amended by Chapter Law 223 to provide for assessment, as part of award against employer, of attorney's fees of employee who is successful in resisting a writ of review by employer, where reviewing court finds "that there is no reasonable basis for the petition." This discourages groundless writs of review by employers.

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